

Committee:	Cabinet	Date:	
Title:	Section 25 - Robustness of Reserves and Adequacy of Estimates 2018/19		15 February 2018
Portfolio Holder:	Cllr Simon Howell, Cabinet Member for Finance and Administration		
Report Author:	Angela Knight, Assistant Director – Resources 01799 510446	Key decision:	No

Summary

1. As part of the annual budget setting process, the Section 151 Officer is required to give the Council formal advice on the robustness of estimates and the adequacy of reserves. This is so Members can set a budget in full awareness of the risks and uncertainties, and ensure that adequate contingency reserves exist.
2. The advice, known as the “Section 25 report”, is being considered by Cabinet tonight and then by Full Council on 22 February as part of the budget approval process.
3. The Scrutiny Committee reviewed this report on 6 February. Comments from the Committee are presented as a separate item on the agenda.

Recommendations

4. The Cabinet is requested to recommend, for approval by Full Council
 - a. That the Council takes account of the advice in the report when determining the 2018/19 General Fund budget and Council Tax.
 - b. That the Council approves the risk assessment relating to the robustness of estimates as detailed in the report
 - c. That the Council sets the minimum safe contingency level for 2018/19 at £1.402 million in line with the specified calculation detailed in point 9 and this to be held in the Working Balance Reserve.
 - d. That the Council agrees that no transfers to or from the Working Balance should be built into the 2018/19 budget outside of maintaining the minimum safe contingency level.
 - e. That the attached Reserves Strategy is adopted

Financial Implications

5. Included in the body of the report

Background Papers

6. None
Impact
 7.

Communication/Consultation	A comprehensive budget consultation exercise was undertaken with in excess 1,800 responses
Community Safety	No specific implications
Equalities	No specific implications
Health and Safety	No specific implications
Human Rights/Legal Implications	No specific implications
Sustainability	The report is prepared in order to comply with Section 25 Local Government Act 2003
Ward-specific impacts	No specific implications
Workforce/Workplace	No specific implications
	No specific implications

Section 25 report

8. Section 25 of the Local Government Act 2003 requires each local authority, when setting its annual General Fund budget and level of Council Tax, to take account of a report from its Section 151 Officer on the robustness of estimates and adequacy of reserves.
9. This document is the report made under Section 25 by the Director of Finance and Corporate Services, as UDC's Section 151 Officer, applicable to the setting of the General Fund budget and Council Tax for 2018/19.
10. The purpose of this requirement is to ensure that when deciding on its budget for a financial year, a local authority is formally made aware of any issues of risk and uncertainty by the Section 151 Officer. The local authority is then expected to ensure that its budget provides for a prudent level of reserves to be maintained.
11. The Director of Finance and Corporate Services has assessed that the minimum safe contingency level for the Working Balance is £1.402 million. This sum is calculated using the following formula

$$(\text{Total gross service expenditure} + \text{total gross service income} + \text{capital financing costs} + \text{investment income} + \text{investment cost} + \text{recharge to HRA} + \text{HRA share of corporate costs}) \times 2\%$$

12. Section 26 of the Act empowers the Secretary of State to set a minimum level of reserves for which a local authority must provide in setting its budget. Section 26 would only be invoked as a fall back in circumstances in which a local authority does not act prudently, disregards the advice of its Section 151 Officer, and where the financial stability of the Council is at risk.

Basis of advice for the Section 25 report

13. In forming the advice for this report, the Director of Finance and Corporate Services has considered the following:

- The requirement that a safe level of contingency is established and maintained in the Council's Medium Term Financial Strategy
- The degree to which the Council's financial plans are aligned to the Council's statutory obligations, local priorities and policy objectives.
- The adequacy of the information systems underpinning the Council's financial management processes.
- Risks associated with the Council's activities, as identified within the risk register.
- The level of earmarked and ringfenced reserves within the General Fund.
- The degree to which uncertainties exist within the draft 2018/19 budget.

Robustness of Estimates

14. There has been detailed scrutiny, review and challenge of budgets by managers, finance officers and CMT. The aim has been to ensure that the budget is based upon realistic estimates, for example, ensuring that contractual commitments are provided for, salary budgets reflect the approved establishment and current staff in post, and income budgets are based on an assessment of price and demand.

15. No budget can ever be completely free from risk. Necessarily, assumptions are made which means that the budget will always contain an amount of uncertainty.

16. The MTFS has been prepared based on the following principles and assumptions;

I. £50k of unavoidable/statutory growth has been built in annually from 2019/20 and there is no capacity for any further growth without the need for compensating savings.

II. There are no new capital items in 2019/20 and 2020/21 other than those identified in the current 5 year rolling capital programme, unless supported by associated financing income.

III.Strategic Initiatives Fund should maintain a balance of £1m as earmarked contingency funds for the Local Plan and any funds above this level will be subject to the current SIF spending criteria (as detailed in the reserves strategy).

IV.The surplus identified from the 2018/19 budget setting is allocated to the Garden Communities Reserves

V.Any in year surpluses are allocated to the Development Reserve, which is earmarked for future projects, for example, the new depot at Little Canfield.

VI.The MTFs reserve is used as a contingency for the loan repayment relating to the investment made through Aspire (CRP) Ltd.

17. The analysis below sets out the major risks applicable to 2018/19 and an indication of the possible impact.

18. It is not possible to give a precise estimate of the impact of each identified risk. As a general guide, the following broad definitions have been used:

Probability	Low Medium High	Possible, but unlikely Probable Almost certain
Impact	Low Medium High	Possible variance of £5,000 to £20,000 Possible variance of £20,001 to £50,000 Possible variance of over £50,000

Risk item	Probability	Impact	Overall Risk of budget variance
<p>Waste & Recycling – This continues to be one of the most complex financially and at greatest risk of volatility. Fuel costs and disposal costs, particularly around cost of dry recycling disposal are variable. Other budget risks have been identified regarding trade waste and green waste, all of which have income budgets that depend upon accuracy of forecasting activity levels.</p> <p>China has announced that it will be banning foreign waste; this includes mixed plastics, mixed textiles and mixed paper. It is unclear on what impact this will have on the recyclable market but it will change the way these are disposed of and could incur extra costs being passed to councils. The Council has mitigated this risk by using an MRF contractor that separates out different polymers and sells target</p>	Medium	High (adverse or favourable)	Medium

Risk item	Probability	Impact	Overall Risk of budget variance
<p>materials on to processors for manufacture into new polymer products. It is more exposed to world market conditions for other materials however.</p> <p>The Council maintains a Waste Management reserve to mitigate the risk. The budget is based on current disposal costs</p>			
<p>Local Plan – Additional consultancy spend or resources may be needed in order to maintain the Local Plan process to the current timetable; although a Planning Reserve exists to meet additional costs, there has been significant pressure on this and a balance from the Strategic Initiative Reserve has now been earmarked to support the cost of the Local Plan.</p>	Medium	High (adverse)	Medium
<p>Planning appeals. A risk of costs of defending appeals and the meeting of costs awarded against the planning authority. The current position of the Local Plan process raises the risk levels in this area.</p>	Medium	High (adverse)	Medium
<p>Business Rates Appeals. The way in which Business Rates is accounted for increases the risk around the forecasts.</p> <p>The key area of risk still remains with appeals; the 2017 reset of business valuation could lead to further appeals.</p>	Medium	High (adverse)	Medium
<p>75% Business Rates Retention. Due to the uncertainty of the increased responsibilities and the precise funding mechanism, it is still difficult to predict the financial implications of the new scheme.</p>	High	High (adverse or favourable)	High
<p>Savings. Work continues to find ways of achieving the same or improved outcomes at lower cost. It is probable that some savings opportunities will be realized with unbudgeted savings arising in 2018/19. Where budgets have already been reduced because of identified savings, the revised budget level is untested so there is an inherent risk of adverse variances.</p>	Medium	Medium (adverse or favourable)	Medium

Risk item	Probability	Impact	Overall Risk of budget variance
<p>Commercialisation. Creation of Council wholly owned subsidiaries and other income generating projects is providing increased income to support the council with the funding reductions. If the financial return reduces this would have a detrimental effect on the overall financial position of the council.</p>	Low	High (adverse)	Medium
<p>Car Park Income. The budget is based on the existing tariff and charging periods as detailed in the fees and charges section of the budget report. If during the year the Council decides to make changes, this will affect the income. For example if the charging period is shortened, or if the Christmas/New Year free periods are extended, income will reduce.</p>	Medium	Low (adverse or favourable)	Low
<p>Fees & Charges income. If economic conditions deteriorate or demand fluctuates there may be unbudgeted loss of income. Building Control, Planning, Land Charges, Licensing, Lifeline and Food Imports are all income streams where risk of volatility has been noted.</p>	Medium	High (adverse)	Medium
<p>Treasury management. Investment risks are spread between various counterparties including UK banks. In the unlikely event of a banking failure, this could have a serious impact on the Council; this is mitigated by specific limits being applied to each counterparty as a percentage of our total investments.</p>	Low	High (adverse)	Medium
<p>Reforms to Housing & Council Tax Benefit. The Council has approved a Local Council Tax Support Scheme that will require non-vulnerable working age people to contribute to their Council Tax liability.</p> <p>Housing benefit reforms and benefit caps have had an adverse impact on amount of claimants benefit awards and this could have an impact on collection rates and increased claims for discretionary housing payments.</p>	Medium	Medium (adverse)	Medium

Risk item	Probability	Impact	Overall Risk of budget variance
<p>Universal Credit – This has now entered the second stage, where all new claimants (excluding Pensioners) now receive Universal Credit (previously only single working age). It was anticipated this would reduce the level of support and administration of Housing Benefits required. Implications are primarily around the Working Balance level.</p> <p>The administration of UC, with significant delays in housing payments being issued has led to a rise in both rent arrears and could led to an increase in homelessness.</p>	Medium	Medium (adverse)	Medium
<p>Supplies & Services contracts. Where contracts have indexation clauses, estimates have been made of the inflationary increase that will be applied. In addition some contracts are due to be re-tendered during the year which could affect the base price. Accordingly there is an inherent risk of price volatility.</p>	Medium	Medium (adverse or favourable)	Medium
<p>Capital Financing costs. These are influenced by variable factors such as cash flow, variations in the Capital Programme and availability of capital receipts. In some circumstances greater revenue financing of capital expenditure may make economic sense over the longer term.</p>	Medium	Low (adverse or favourable)	Low

19. Taking all of the above issues into consideration, the Director of Finance and Corporate Services is unable to provide a full assurance that there will be no unforeseen variances. This is an expected and acceptable situation for any organisation that has to deal with a large number of variables. Provided that the minimum safe level of balances is maintained (as set out in the attached Reserves Strategy), any variations arising as a result of any lack of robustness in the estimates should be manageable.

20. The risks identified will be proactively monitored and mitigating action taken as soon as reliable trends emerge. Budget monitoring reports will be presented to Members at quarterly intervals during the financial year, which will set out the latest financial position and action being taken, where applicable.

Adequacy of reserves

21. Attached is the Reserves Strategy which sets out the purpose, risks and calculation for each reserve held by the council.

22. It is the opinion of the Director of Finance and Corporate Services that the reserves as set out in the Strategy are adequate and appropriate.

Risk Analysis

23.

Risk	Likelihood	Impact	Mitigating actions
Actual events may differ from the assumptions and estimates used to produce the draft budget, which will lead to variances from the budget.	4 (variances will occur requiring action to be taken)	3 (potential impact which could adversely affect the council's financial position if not managed)	Budget monitoring and corrective action taken as necessary. Maintain sufficient reserves and Working Balance.

1 = Little or no risk or impact

2 = Some risk or impact – action may be necessary.

3 = Significant risk or impact – action required

4 = Near certainty of risk occurring, catastrophic effect or failure of project.